

Message Text

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TREAS DEPT WASHDC IMMEDIATE
INFO AMEMBASSY PARIS IMMEDIATE
AMEMBASSY BONN
AMEMBASSY LONDON

C O N F I D E N T I A L SECTION 1 OF 2 ROME 3070

LIMDIS GREENBACK

PARIS FOR USOECD (PASS SOLOMON)

E.O. 11652: GDS
TAGS: EFIN, IT
SUBJ: VISIT OF TREASURY UNDER SECRETARY SOLOMON

1. SUMMARY. DURING HIS VISIT TO ROME, TREASURY UNDER SECRETARY SOLOMON EXCHANGED VIEWS WITH ITALIAN OFFICIALS ON THE WORLD ECONOMIC SITUATION, RESULTS OF G-5 MEETING, US EXCHANGE RATE POLICY AND TRADE ISSUES. HE ALSO RECEIVED BRIEFING ON ITALY'S ECONOMIC SITUATION AND OUTLOOK. END SUMMARY.

2. DURING HIS BRIEF STOP-OVER IN ROME FEBRUARY 14-15, TREASURY UNDER SECRETARY SOLOMON HAD OCCASION TO MEET WITH SEVERAL HIGH-LEVEL ITALIAN OFFICIALS IN THE COURSE OF A DINNER AND LUNCHEON HOSTED BY AMBASSADOR GARDNER. THE DINNER ON FEBRUARY 14 WAS ATTENDED BY MINISTERS STAMMATI AND PANDOLFI, GOVERNOR OF BANK OF ITALY BAFFI AND DIRECTOR GENERAL PALUMBO (TREASURY) AND ERCOLANI (BANK
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OF ITALY). THE LUNCHEON ON FEBRUARY 15 WAS ATTENDED BY GUIDO CARLI (PRESIDENT OF CONFIDUSTRIA), GIANNI AGNELLI (PRESIDENT OF FIAT) AND RINALDO OSSOLA (MINISTER OF FOREIGN TRADE).

3. DURING THE CONVERSATIONS, UNDER SECRETARY SOLOMON MADE THE FOLLOWING MAJOR POINTS:

(A) US ECONOMIC OUTLOOK. THE UNDER SECRETARY SAID THE GROWTH RATE IN THE US IN 1978 WILL PROBABLY BE AROUND 4.75 PERCENT AS COMPARED WITH 3.5 PERCENT FOR THE EUROPEAN COUNTRIES. THIS REPRESENTED A SIGNIFICANT NARROWING OF THE GROWTH SPREAD BETWEEN THE US AND THE EUROPEANS, WHICH WOULD BENEFIT THE US CURRENT ACCOUNT. HE SAW, HOWEVER, ONLY SLIGHT IMPROVEMENT IN THE US CURRENT ACCOUNT IN 1978, EVEN THOUGH OIL IMPORTS ARE NOT EXPECTED TO SHOW ANY INCREASE OVER 1977. SOLOMON GAVE A GENERALLY UPBEAT REPORT OF THE US ECONOMY.

(B) RESULTS OF G-5 MEETING. SOLOMON INDICATED THAT THE MEETING REVEALED A GREAT DEAL OF CONVERGENCE ABOUT THE 1978 ECONOMIC TARGETS OF THE PARTICIPATING COUNTRIES. HE NOTED THAT THE MEETING IN BONN WITH CHANCELLOR SCHMIDT WAS VERY POSITIVE, THAT GERMAN ECONOMY WAS NOW MOVING IN RIGHT DIRECTION AND THAT THE US AND GERMANY WERE IN BASIC AGREEMENT.

(C) EXCHANGE MARKETS. US INTERVENTION POLICY WAS DESIGNED TO SMOOTH OUT DISORDERLY CONDITIONS AND THE POLICY WAS COORDINATED WITH OTHER COUNTRIES. SOLOMON STRESSED THAT, DESPITE THE LARGE REVALUATION OF THE DEUTSCHMARK AND YEN, ON A TRADE-WEIGHTED BASIS THE DOLLAR HAD NOT LOST MUCH GROUND. SOLOMON EMPHASIZED

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THAT THE US DOES NOT, REPEAT NOT, EXPECT TO ELIMINATE ITS CURRENT ACCOUNT DEFICIT THROUGH THE EXCHANGE RATE MECHANISM. IN RESPONSE TO A QUESTION, HE SAID THE US HAD NO INTENTION OF ISSUING FOREIGN CURRENCY DENOMINATED SECURITIES SINCE THE WEAKNESS OF THE DOLLAR WAS A TEMPORARY PHENOMENON.

(D) TRADE ISSUES. ON STEEL, SOLOMON EXPLAINED RATIONALE FOR INTRODUCTION FOR TRIGGER PRICE SYSTEM, POINTED OUT THAT IT OFFERED ADVANTAGES OVER OTHER ALTERNATIVES TO EUROPEAN PRODUCERS AND THAT IT HAD GAINED GENERAL ACCEPTANCE OF US INDUSTRY AND THE CONGRESS. WITH RESPECT TO MTN, SOLOMON STRESSED IMPORTANCE OF CONCLUDING AGREEMENTS ON SERIES ON NON-TARIFF MEASURES. IN PARTICULAR, HE DESCRIBED PROBLEMS RELATING TO US COUNTERVAILING DUTY STATUTE AND RESULTING NEED TO ARRIVE AT AGREEMENT ON SUBSIDIES BY END OF YEAR. HE HOPED GOI WOULD RAISE VOICE OF URGENCY ON THIS ISSUE IN EC COUNCILS.

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C O N F I D E N T I A L SECTION 2 OF 2 ROME 3070

LIMDIS GREENBACK

PARIS FOR USOECD (PASS SOLOMON)

4. DURING THE DISCUSSIONS, ITALIAN OFFICIALS MADE THE
FOLLOWING POINTS:

(A) BAFFI. REFERRING TO THE ENLARGED BUDGET DEFICIT OF
THE PUBLIC SECTOR FOR 1978 AND TO THE FACT THAT THE
SIZE OF THAT DEFICIT WILL BE PRETTY MUCH FIXED BY THE
TIME THE IMF MAKES ITS REVIEW IN MARCH OR APRIL, BAFFI
STATED THAT THE FUND COULD IMPOSE CONDITIONS ON HOW
THAT DEFICIT IS FINANCED. HE SEEMED TO HAVE TAKEN IT
FOR GRANTED THAT THE DEFICIT WOULD BE AROUND 24,000
BILLION LIRE.

(B) PANDOLFI. DISCUSSING POSSIBILITIES AND PROBLEMS
WITH REDUCING THE BUDGET DEFICIT BY INCREASING REVENUES,
PANDOLFI BELIEVED THE ONLY AVENUE OPEN FOR 1978
WAS THAT OF INDIRECT TAXES, PARTICULARLY IVA. (DIRECT
TAXES CANNOT BE ADJUSTED AT MID-YEAR FOR IMPACT IN THE
SAME YEAR.) PANDOLFI WAS CONCERNED, HOWEVER, WITH THE
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INFLATIONARY CONSEQUENCES OF INCREASING IVA AND
SUGGESTED THAT THE NEXT GOVERNMENT SHOULD ASSESS THE

POSSIBILITY OF EXCLUDING SOME INDIRECT TAXES FROM THE SCALA MOBILE.

(C) STAMMATI. THE MINISTER INDICATED THAT ITALY PLANS TO MEET IN FULL ITS FOREIGN DEBT OBLIGATIONS FOR 1978. WITH RESPECT TO PUBLIC SECTOR SPENDING, HE SAID HE FAVORED ELIMINATING THE DOUBLE INDEXATION OF PENSIONS WHICH IS NOW POSSIBLE SINCE PENSIONS ARE ADJUSTED ON THE BASIS OF THE SCALA MOBILE AND ADJUSTMENTS IN THE MINIMUM WAGE.

(D) OSSOLA. OSSOLA SAID IT WAS "UNTHINKABLE" THAT GOI MIGHT BE UNABLE TO CONCLUDE A STANDBY WITH THE IMF. HE SAID HE THOUGHT THE IMF WOULD ACCEPT 1978 PUBLIC DEFICIT AT LIRE 24,000 (OR "24 MEGALIRE") BUT COUPLED WITH ACTION TO REDUCE THAT AMOUNT IN 1979. OSSOLA ALSO FLOATED IDEA OF STANDBY ESTABLISHING RANGES RATHER THAN TARGETS IN THE VARIOUS CATEGORIES AND POSSIBLY INCLUDING PROVISION FOR TRADE-OFFS AMONG THESE RANGES. ON TRADE ISSUES, OSSOLA REPORTED CONSIDERABLE SUCCESS IN DENDING OFF DOMESTIC PROTECTIONIST PRESSURES AND NOTED SOLOMON'S CONCERNS ON SUBSIDY ISSUE.

(E) CARLI. IDENTIFYING CONTINUED RISE IN REAL WAGES FASTER THAN PRODUCTIVITY AS MAJOR CONTRIBUTOR TO ITALY'S ECONOMIC ILLS, CARLI EXPRESSED SKEPTICISM ABOUT APPARENT CHANGE IN ATTITUDE OF LABOR UNIONS, INDICATING THAT CRUCIAL TEST WOULD COME WHEN UNIONS GOT DOWN TO SPECIFICS. CARLI THEN ZEROED IN ON PROBLEM OF PUBLIC EXPENDITURES. HE STRESSED FOUR KEY AREAS WHERE ACTION IS REQUIRED: PENSIONS, WHICH ARE HEADED FOR DISRUPTIVE

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INCREASE IN 1979; HEALTH COSTS, WHICH ARE ENORMOUS PERCENTAGE OF GNP; INTEREST PAYMENTS; AND LOCAL GOVERNMENT, WHERE AT LEAST SOME ACTION IS BEING TAKEN.

(F) AGENLLI. ON POLITICAL SITUATION, AGNELLI ASSERTED THAT PCI ENTRY INTO PARLIAMENTARY MAJORITY WOULD NOT, IN FACT, REPRESENT MAJOR CHANGE OVER EXISTING SITUATION BUT WOULD BE PERCEIVED AS SUCH. SINCE THIS WOULD CAUSE SHOCK, BOTH DOMESTICALLY AND INTERNATIONALLY, THE DC SHOULD COMPENSATE FOR THAT BY ADOPTING A TOUGH ECONOMIC PROGRAM. AGENLLI ALSO EXPRESSED VIEW THAT VICTORY OF THE LEFT IN FRANCE WOULD ENSURE PCI ENTRY INTO THE GOVERNMENT. WHILE THAT WOULD PRESUMABLY COME AFTER PARLIAMENTARY ELECTIONS, IT WOULD ESSENTIALLY BT AT A TIME OF PCI'S CHOOSING.

5. IN EMBASSY'S VIEW, SOLOMOM'S VISIT WAS EXTREMELY

USEFUL IN ENABLING TOP ITALIAN LEADERS FROM GOVERNMENT
AND PRIVATE SECTOR TO HEAR FIRST-HADN DESCRIPTION OF
US POLICIES AND REPORT ON CERTAIN INTERNATIONAL
DEVELOPMENTS AS WELL AS FOR US TO OBTAIN ITALIAN LEADERS'
VIEWS ON DOMESTIC AND FOREIGN ISSUES AFFECTING ITALY.
GARDNER

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